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No. 80-

IN THE

Supreme Court of the United States

EDITH M. MARSCHAK, etc., *et al.*

Petitioner,

vs.

KIRKLAND and ELLIS, a Partnership, and
WESTINGHOUSE ELECTRIC CORPORATION,

Respondents.

PETITION FOR WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE SEVENTH CIRCUIT

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QUESTIONS PRESENTED

For the purposes of determining diversity of citizenship in a derivative shareholders action:

I. If there is no allegation of wrongdoing against corporate management, is denial of realignment of the corporation as a party plaintiff justified on the basis of antagonism presumed to exist merely because the corporation did not file suit in response to the shareholders' Rule 23.1 demand?

II. Is the determination of whether the corporation is antagonistic to the suit to be made on the basis of the complaint and any responsive pleading, or in an inquiry considering proceedings extrinsic to these initial pleadings.

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PETITION FOR WRIT OF CERTIORARI
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Petitioner Edith M. Marschak,[1] prays that a writ of certiorari issue to reverse the judgment of the United States Court of Appeals For The Seventh Circuit entered on July 21, 1980. A petition for rehearing was denied on September 17, 1980.

[1] Edith M. Marschak, now known as Edith M. Ashley, is a trustee of a family trust that has held Westinghouse stock through all times relevant to the complaint. She sues in a derivative capacity.

OPINIONS

The opinions below, which have not been reported, are set out in the Appendices to this Petition. The opinion of the Court of Appeals is Appendix A; the opinion of the trial court, and its reconsideration, is Appendix B.

JURISDICTION

This Court has jurisdiction under 28 U.S.C. Sec. 1254(1). The Court of Appeals rendered its opinion on July 21, 1980. A timely petition for rehearing was denied on September 17, 1980. The Court of Appeals had jurisdiction under 28 U.S.C. Sec. 1291 of an appeal from the District Court for The Northern District of Illinois, Eastern Division. Plaintiff claimed jurisdiction in the District Court on the basis of diversity of citizenship, 28 U.S.C. Section 1332.

STATUTES AND RULES INVOLVED

28 United States Code Section 1332:

> "(a) The district courts shall have original jurisdiction of all civil actions where the matter in controversy exceeds the sum or value of $10,000, exclusive of interest and costs, and is between—
>
> (1) citizens of different States;
>
> * * *
>
> "(c) For the purposes of this section and section 1441 of this title, a corporation shall be deemed a citizen of any State by which it has been incorporated and of the State where it has its principal place of business: * * *"

Federal Rules of Civil Procedure 23.1:

> "In a derivative action brought by one or more shareholders or members to enforce a right of a corporation or of an unincorporated association, the corporation or association having failed to enforce a right which may properly be asserted by it, * * * the complaint shall also allege with particularity the efforts, if any, made by the plaintiff to obtain the action he desires from the directors or comparable authority . . . and the reasons for his failure to obtain the action. . . ."

STATEMENT OF THE CASE

Nature of the Litigation

In this derivative shareholders action, the shareholder seeks recovery for the Westinghouse Electric Corporation against Kirkland & Ellis, its former attorneys, disqualified by the Court of Appeals in *Westinghouse* v. *Kerr-McGee, Gulf Oil Corp. and Getty Oil Co.,* 580 F.2d 1311 (7th Cir.), *cert. denied,* 439 U.S. 955 (1978). The Court found that Kirkland and Ellis had been guilty of a conflict of interest, having simultaneously represented defendants as well as Westinghouse as the plaintiff in a certain Uranium anti-trust case. The derivative action seeks recovery for Westinghouse of all fees which were charged by the law firm during the period of the conflict of interest, estimated to be approximately $2,500,000, 580 F.2d at 1313.

The Grounds for Realignment of the Corporation as a Party Plaintiff, and the Motion To Dismiss for Lack of Diversity of Citizenship Jurisdiction

The suit is brought under diversity of citizenship, 28 U.S.C. § 1332. The shareholder, Edith M. Marschak, (an Illinois citizen) brings suit as a nominal plaintiff, on behalf of Westinghouse, (a Pennsylvania corporation) against Kirkland and Ellis (an Illinois partnership). In response to a motion to dismiss for lack of complete diversity of citizenship, the shareholder requested the trial court to realign Westinghouse as a party plaintiff, and to disregard her citizenship, for the purpose of determining diversity of jurisdiction.

There are no allegations of wrongdoing on the part of Westinghouse management; Westinghouse did not oppose the action in its response to the shareholder's Rule 23.1 demand. However, the District Court below refused to order Westinghouse realigned as a party plaintiff, and granted West-

inghouse's motion to dismiss the complaint[2] for lack of complete diversity of jurisdiction.

The Rule 23.1 demand is set out in full in Appendix C. As noted above, it did not make allegations of wrongdoing against Westinghouse or its management.

The Corporation's answer to the demand is set out in full in Appendix D. It stated that Westinghouse, too, wanted to investigate the claim against Kirkland and Ellis, and that it had engaged Eckert, Seamans, a Pittsburgh law firm, to do so. The Eckert firm, however, was disqualified from undertaking the work because for over twenty years it had represented both Westinghouse and the Gulf Oil Corporation, the parties which had been represented by Kirkland and Ellis in the Uranium litigation. This was the reason, as contemplated by Rule 23.1, that the shareholder, therefore, upon receipt of the Westinghouse answer, proceeded to file this action. The answer to the demand was made part of the complaint (par. 4(a)) in an amendment, pursuant to F.R.C.P. 15. Defendants moved to dismiss, asserting lack of complete diversity of citizenship.

Thus on the complaint—the motion to dismiss was on procedural grounds, and not on the merits—the record showed inaction by the Corporation, but not antagonism. The Court of Appeals, however, in affirming the decision of the trial court, inferred antagonism from the mere fact that the Corporation did not file the action in response to the demand. The Court also took the demand itself as a sign of antagonism, even though the language of the demand did no more than follow the requirements of Rule 23.1.

In deciding whether to align Westinghouse as defendant or plaintiff, the District Court did not limit its inquiry to the complaint. The Court looked to subsequent proceedings, which

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[2] All pleadings, memoranda, briefs and arguments of Westinghouse were adopted by Kirkland and Ellis in the trial and reviewing court.

occurred months after the action was initiated, and perceived antagonism both from the shareholder's opposition to defendants' efforts to a stay of discovery, and the shareholder's motion to disqualify a Special Investigation Committee, which had been appointed by the Corporation, for lack of the requisite independence.

The Committee had not been appointed until after the suit was filed. The shareholder moved to disqualify the Committee for lack of the requisite independence as it was represented in the proceedings below by counsel for Westinghouse, and as Westinghouse's counsel participated in the Committee's onvestigation and deliberations. The Committee, however, in behalf of the Corporation, remained neutral throughout the proceedings.

The trial court did not rule on the motion, and the Committee did not make any recommendation to the Corporation on the action prior to dismissal of the complaint.

The Court of Appeals affirmed. In doing so, it concluded that the Corporation's failure to act was the same as a collision of issues between the shareholder and the Corporation, that even though the Corporation, through its Special Investigation Committee, was neutral, there was "antagonism" because of the Corporation's mere inaction.

The record stands that without allegations of wrongdoing against corporate management, the Corporation was not aligned as a party plaintiff, as though there would always be hostility between the shareholder and the Corporation in an ordinary derivative action where the shareholder brought suit after a corporation merely failed to act on a Rule 23.1 demand.

REASONS FOR GRANTING THE WRIT

INTRODUCTION

Ordinarily, a corporation will be aligned as a party plaintiff in a derivative action brought on its behalf as it is the real party in interest. However, if the shareholder charges malfeasance against corporate management, equity gives "special dispensation" to the corporation, and allows it to defend, rather than join in, such claims. The corporation and the shareholder are "antagonistic." *Koster* v. *Lumbermans Mutual Cas. Co.,* 330 U.S. 518, 522-523 (1947). Following this reasoning in *Smith* v. *Sperling,* 354 U.S. 91 (1957), and a companion case, *Swanson* v. *Traer,* 354 U.S. 114 (1957), this Court set down the procedure for making this determination.

In the present case, the decision below conflicts with this Court's procedural ruling. But of even broader significance, the Court below has applied this Court's definition of antagonism based on the charges of malfeasance against corporate officers to any derivative action where the corporation does not sue, as though its failure to do so is to be equated with antagonism. That aspect of the decision conflicts with the decision of the Second Circuit in *Lewis* v. *Odell,* 503 F.2d 445, 446-447 (2d Cir. 1974), discussed below.

I. FINDING ANTAGONISM BY MANAGEMENT MERELY FOR REFUSING TO FILE SUIT ON A SHAREHOLDER'S RULE 23.1 DEMAND MISAPPLIES THE PRESUMPTION OF ANTAGONISM BASED ON CHARGES OF WRONGDOING BY CORPORATE MANAGEMENT, WHICH DOES NOT APPLY IN AN ORDINARY DERIVATIVE ACTION FILED ON THE CORPORATION'S BEHALF.

The ruling below makes any derivative action antagonistic and prevents a corporation ever from being aligned as a party plaintiff where the corporation does not sue.

The Court's substantive rulings in *Koster, Smith* and *Swanson* follows a venerable line of cases in which the finding of antagonism was based on charges of malfeasance—fraud, breach of trust or illegality, *Central R. Co.* v. *Mills,* 113 U.S. 249, (1885), and *Doctor* v. *Harrington,* 196 U.S. 579, (1905). However, this Court has never ruled that mere refusal to sue in a case brought solely for the corporation's benefit is to be equated with a grounds for a finding of antagonism.

This question is of broad significance because if the decision below is allowed to stand, in any derivative shareholders action there will automatically be a finding of antagonism, even if the corporation does no more than fail or refuse to file in response to a typical Rule 23.1 demand, and if once the suit is filed the parties engage in ordinary procedural motions, none of which put the corporation on record as opposing the suit.[3]

The decision below conflicts with the ruling of the Second Circuit.

Lewis v. *Odell,* 503 F.2d 445, 446-447 (2d Cir. 1974), realigned the Corporation as a party plaintiff, and the citizenship of the plaintiff shareholder became irrelevant to the consideration of diversity jurisdiction.[4] The corporation was in bankruptcy, its trustees (who were then its management) would not be harmed by the suit and the company had been neutral to the action. The pleadings did not disclose the requisite antagonism of charges against management, and the

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[3] In this case the corporation did not oppose the suit. Its Special Investigation Committee, appointed after suit was filed to investigate, was by definition neutral. It did not make a recommendation to the corporation until after the trial court granted the motion to dismiss. There is nothing in the record as to whether the Corporation ever considered the recommendation.

[4] The shareholder is a nominal party, dissent of Justice Frankfurther, *Smith* v. *Sperling,* 354 U.S. at p. 97; *Ross* v. *Bernhard,* 396 U.S. 531, 538 (1970); *Koster, supra,* at p.522.

Court held there was no antagonism. The Second Circuit, relied on *Smith* v. *Sperling* and *Swanson* v. *Traer,* 503 F.2d at 447. Thus there is a direct conflict between the Circuits on this point which should be resolved by this Court.

II. THE DETERMINATION OF ALIGNMENT OF A CORPORATION AS PLAINTIFF OR DEFENDANT IN A DERIVATIVE ACTION IS TO BE MADE NOT ON THE BASIS OF PROCEEDINGS MONTHS AFTER THE SUIT IS FILED, BUT ON THE FACE COMPLAINT AND ANY RESPONSIVE PLEADING.

The ruling below resurrects uncertainty in the process of determining diversity jurisdiction in derivative actions.

The decision of the Court of Appeals conflicts with this Court's procedural ruling in *Smith* v. *Sperling* and *Swanson* v. *Traer.*[5] The Court of Appeals erroneously upheld a procedure

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[5] *Smith* v. *Sperling,* at p. 96:

"The bill and answer normally determine whether the management is antagonistic to the stockholder . . . "

The Court cited *Central R. Co.* v. *Mills,* 113 U.S. 249 (1885) and *Doctor* v. *Harrington,* 196 U.S. 579 (1905), and referred to *Hawes* v. *Oakland,* 104 U.S. 450 (1881), stating (354 U.S. at p. 96, fn. 3):

" . . . where in determining whether a proper case for a derivative action had been made out, the Court looked *only to the nature of the charges contained in the bill. Id.* 104 US pp. 461, 462." (Emphasis by the Court)

The procedure approved of below, looking to events subsequent to the filing of the action, conflicts with the decision of Chief Justice Marshall in *Mollan* v. *Torrance* (US) 9 Wheat 537, 539 (1824):

"It is quite clear, that the jurisdiction of the court depends upon the state of things at the time of the action brought, and that after vesting, it cannot be ousted by subsequent events."

The Court in *Smith* v. *Sperling,* 354 U.S. at p. 115, characterized the determination to be one "on the issues of wrongdoing" where there were such charges against corporate management.

going beyond an examination of the complaint and any responsive pleading. Instead the Court approved an inquiry which examined motions made months after the filing of those initial documents, and which would resurrect the uncertainty in such proceedings struck down by this Court in the *Smith* and *Swanson* decisions. The Court below erroneously relied on *Indianapolis* v. *Chase Nat. Bank,* 314 U.S. 63 (1941). In that case the interest of the corporation and trustees bring suit was common. Therefore, realignment of the corporation as plaintiff had been error, at p. 74. However, but for the common interest, it is clear that the realignment of the corporation would have stood; there was no claim of wrongdoing by corporate management. And although the Court of Appeals now speaks to the contrary (App. A. p7a), it has previously ruled in *Hoefferle Truck Sales* v. *Divco-Wayne,* 523 F.2d 543, 548 (1975) that: "It is fundamental that diversity is determined as of the time suit is commenced. *Julian* v. *Sarkas Tarzian, Inc.,* 352 F.2d 845, 846 (7th Cir. 1965)." That was correct.

CONCLUSION

For the reasons stated in this petition for a writ of certiorari, this Court should grant review, and order the decision below reversed, and the complaint reinstated.

Respectfully submitted,

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APPENDIX A

UNITED STATES COURT OF APPEALS

For the Seventh Circuit

Chicago, Illinois 60604

(Argued April 14, 1980)

July 21, 1980

Before

Hon. THOMAS E. FAIRCHILD, Chief Judge

Hon. WALTER J. CUMMINGS, Circuit Judge

Hon. WILLIAM J. JAMESON, Senior District Judge*

EDITH M. MARSCHAK, now known as EDITH M. ASHLEY, as Trustee, on behalf of herself, in such capacity, and on behalf of others similarly situated,

Plaintiff-Appellant,

No. 79-2464 *vs.*

KIRKLAND and ELLIS, a partnership, and WESTINGHOUSE ELECTRIC CORPORATION,

Defendants-Appellees.

Appeal from the United States District Court for the Northern District of Illinois, Eastern Division.

No. 79 C 1579

Honorable Frank J. McGarr, Judge Presiding.

ORDER

Appellant, Edith Marschak, brought this shareholder derivative action on behalf of herself, as trustee, and all other shareholders of Westinghouse Electric Corporation, (Westinghouse), [1] naming as defendants Westinghouse and Kirkland and Ellis, an Illinois partnership engaged in the practice of law. The district court dismissed the action for lack of subject matter jurisdiction because appellant failed to establish diversity of citizenship under 28 U.S.C. § 1332. We affirm.

* The Honorable William J. Jameson, United States Senior District Judge for the District of Montana, is sitting by designation.

[1] Appellant is trustee of a trust which owns stock in Westinghouse.

Background

By letter dated March 13, 1979, appellant's attorney wrote Westinghouse's Board of Directors demanding that the corporation institute an action "with immediate dispatch" against Kirkland and Ellis for the recovery of legal fees, costs and damages incurred by Westinghouse in *Westinghouse Electric Corp.* v. *Kerr-McGee Corp., Gulf Oil Corp. and Getty Oil Co.*,[2] by reason of the fact that the law firm had been found to be disqualified from representing Westinghouse because of a conflict of interest. The letter stated further that unless appellant was assured within 30 days that litigation would be undertaken by Westinghouse, appellant would institute a derivative action. By letter dated April 9, Westinghouse informed appellant's attorney that it had commenced an investigation through independent counsel and that the Board was currently reviewing the results of that investigation.

On April 19, 1979, appellant filed this action, alleging service of the demand letter, pursuant to Rule 23.1, F.R. Civ.P.[3]; that Westinghouse "responded but failed to take appropriate action"; that further demand would be futile; and that "plaintiffs have no remedy except as requested from this court". The complaint alleged that appellant was a "nominal party, the defendant corporation being the real party in interest", and that the district court "has jurisdiction under 28 U.S.C. 1332 as there is a diversity of citizenship between the Corporation which has its principal place of business in Pittsburg, Pennsylvania, and the defendant, an Illinois partnership entity'". There was no allegation with respect to appellant's citizenship.

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[2] This court's opinion is reported at 580 F.2d 1311 (7 Cir.) *cert. denied,* 439 U.S. 955 (1978).

[3] F.R.Civ.P. 23.1, "Derivative Actions by Shareholders", requires that, "The complaint shall . . . allege with particularity the efforts, if any, made by the plaintiff to obtain the action he desires from the directors or comparable authority. . . ."

On April 25, 1979, Westinghouse's Board of Directors established a Special Investigation Committee "to consider whether the prosecution of the claims alleged on behalf of the Corporation in the Derivative Actions[4] would be in the best interests of the Corporation and its shareholders". Westinghouse later moved to stay the proceedings in appellant's derivative action, including discovery requests by appellant, pending the outcome of the investigation. Appellant then moved to advance discovery and to stay the proceedings of the Special Investigation Committee. Appellant also amended her complaint, alleging that "to await action by the Corporation would have been futile" because certain members of the Special Investigation Committee also had a conflict of interest.

Westinghouse moved for dismissal on the grounds that (1) the complaint failed to aver facts sufficient to show diversity; and (2) on the basis of its belief that plaintiff was an Illinois citizen, diversity jurisdiction was lacking because the defendant, Kirkland and Ellis, was also an Illinois citizen. Appellant resisted the motion by arguing (1) that she was a nominal party, and therefore, her state of citizenship was irrelevant and (2) that Westinghouse should be realigned as a plaintiff. The district court rejected appellant's contentions and issued a memorandum opinion and order finding diversity of citizenship lacking and dismissing the complaint without prejudice. The court also refused to grant appellant's motion for leave to send a notice to other shareholders advising them of the dismissal and inviting them to substitute as plaintiffs. On appeal, appellant argues that the district court erred in both rulings.

Diversity of Citizenship

As the district court correctly stated in its memorandum opinion:

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[4] There was a second derivative action not related to this action.

> It is well settled that whenever federal jurisdiction is based on diversity of citizenship under 28 U.S.C. § 1332 (1976), there must be complete diversity. "That is, diversity jurisdiction does not exist unless *each* defendant is a citizen of a different State from *each* plaintiff." *Owen Equipment & Erection Co.* v. *Kroger,* 437 U.S. 365, 373 (1978) (emphasis in original). The burden of proving jurisdiction is, of course, on the party seeking to invoke the court's jurisdiction. Likewise, when diversity is challenged the burden remains on the party who has alleged diversity. *Village Fair Shopping Center Co.* v. *Sam Broadhead Trust,* 588 F.2d 431, 433 (5th Cir. 1979).

In determining whether diversity jurisdiction exists, the alignment of the parties as set forth in the pleadings is not, of course, conclusive. Rather, the court must "look beyond the pleadings and [should] arrange the parties according to their sides in the dispute". *Dawson* v. *Columbia Trust Co.,* 197 U.S. 178, 180 (1905); *Indianapolis* v. *Chase Nat'l Bank,* 314 U.S. 63, 69 (1941). The ultimate "interests" of the parties determine their sides in the lawsuit. In a stockholder's derivative suit, the ultimate interests of the stockholder and the corporation will generally be the same. Where, however, the management is definitely opposed to the institution of the litigation, it is "antagonistic" to the stockholders, and the parties will be aligned on opposite sides of the dispute. See, *e.g., Smith* v. *Sperling,* 354 U.S. 91 (1957); *Swanson* v. *Traer,* 354 U.S. 114 (1957); *Doctor* v. *Harrington*), 196 U.S. 579 (1905).

In its memorandum opinion, the district court noted that the complaint failed to "indicate plaintiff Marschak's state of citizenship [and failed to] indicate defendant Westinghouse's state of incorporation, which is one determinant of a corporation's citizenship". It concluded that, "Because jurisdiction is based only on diversity of citizenship, the complaint is defective for failing to allege the parties' citizenship." The court continued:

> The court cannot realign Westinghouse and ignore plaintiff Marschak's citizenship. Realigning the corporation in derivative suits is proper only when it is clear that the cause of action belongs to the corporation and the corporation is not antagonistic to the shareholder. To determine whether there is antagonism between the corporation and the shareholder, the court looks only at the pleadings. *Smith* v. *Sperling,* 354 U.S. 91 (1957).

The district court concluded that it was clear from the pleadings that appellant's "view of any action differs from the Board of Directors' view". Sufficient antagonism to preclude realignment was shown (1) by plaintiff's amended complaint which alleged the Board's action against Kirkland and Ellis was inadequate; and (2) by plaintiff's motion to disqualify the Special Investigation Committee, which was appointed to determine whether Westinghouse should assert a claim against Kirkland and Ellis. The court concluded that since Westinghouse could not be realigned, plaintiff could not be considered a nominal plaintiff and her citizenship was relevant. Plaintiff did not refute Westinghouse's assertion that she was an Illinois resident.[5] Therefore, "Because defendant Kirkland also had Illinois citizenship, complete diversity is lacking."

Appellant contends the district court erred "in finding antagonism between the shareholder and the corporation, either on her demand, as of the time of the filing of the complaint as amended, or subsequently, when she challenged the Special Investigation Committee for lack of independence". She argues (1) that under *Smith* v. *Sperling, supra,* antagonism "against the demands of the shareholder is to be found only if there is some clear and unequivocal indication by the corporation that it opposes the shareholder's action"; (2) that Westinghouse's answer to her demand that it too was looking

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[5] The court noted that, "While residency is not synonymous with citizenship, proof of residency is prima facie evidence of citizenship absent any indication to the contrary," citing C. Wright, A. Miller, and E. Cooper, Federal Practice and Procedure, § 3611 at 711-12.

into the matter and its subsequent appointment of a Special Investigation Committee shows there was no antagonism; and (3) that the district court was prohibited from considering her motion to disqualify the Special Investigation Committee since antagonism is to be determined "at the time the complaint is filed [or] . . . amended". We disagree.

While the record must show that the corporate management opposes the institution of litigation to make it "antagonistic", see *Swanson* v. *Traer, supra,* this opposition may be shown by the management's failure to act for any reason. As the Court stated in *Smith* v. *Sperling, supra,*

> The management may refuse or fail to act for any number of reasons. Fraud may be one; the reluctance to take action against a close business associate may be another; honest belief in the wisdom of the course of action which the management has approved may be still another; and so on.

Id. at 96.

The Court continued:

> The attitude of the directors need not be sinister. It may be sincere. Whenever the management refuses to take action to undo a business transaction or whenever, as in this case, it so solidly approves it that any demand to rescind would be futile, antagonism is evident. The cause of action, to be sure, is that of the corporation. But the corporation has become through its managers hostile and antagonistic to the enforcement of the claim.

Id. at 97 (quoting from *Delaware & H. Co.* v. *Albany & S. R. Co.,* 213 U.S. 435).

We agree with the district court that the response of Westinghouse's Board of Directors to appellant's suit showed sufficient antagonism to preclude realignment. It appears from the face of the complaint that (1) the corporation "failed to take appropriate action on her demand" to bring suit against Kirkland and Ellis, (2) further demand would be "futile" and

"unavailing"; (3) "*independent action is necessary*" because Westinghouse continued to retain Kirkland and Ellis after the conflict of interest was exposed and Westinghouse has a record of "conflicts of interest with its counsel" (emphasis added); (4) the counsel Westinghouse engaged to look into the questions also have a conflict of interest; and (5) because of these circumstances, the stockholders' "*only recourse* was to seek relief from this court" (emphasis added). In light of these allegations and the fact that Westinghouse is resisting appellant's action, it would be anomalous to hold that the Board of Directors is not "hostile and antagonistic to the claim", (citing *Smith* v. *Sperling,* 354 U.S. 91, at 97 (1957)).

Moreover, in examining the nature of the controversy to resolve the antagonism issue it was proper for the district court to consider appellant's motion to disqualify the Special Investigation Committee and other motions and papers filed throughout the proceedings. Although the requirement of diversity of citizenship is ordinarily determined by considering the circumstances as they existed at the time the action commenced, *e.g., Hoefferle Truck Sales, Inc.* v. *Divco-Wayne Corp.,* 523 F.2d 543 (7 Cir. 1975), "in determining whether realignment of parties is required, the position taken by a party during the litigation may be considered in determining how he should originally have been aligned." Wright, Law of Federal Courts § 28, p. 93 (1970); Accord, *Green* v. *Green,* 218 F.2d 130, 144 (7 Cir.) *cert. denied,* 349 U.S. 917 (1954). Professor Wright states further: "Although questions of alignment are determined initially from the pleadings, the subsequent course of the litigation may reveal more clearly the position of the various parties and cast light on how they should have been originally aligned." § 30, p. 97.

Westinghouse moved to stay proceedings in appellant's action, including discovery requests. In turn appellant moved to advance discovery and to disqualify the Special Investigation

Committee. These proceedings "reveal more clearly" that Westinghouse was properly aligned as a defendant when appellant commenced her action.[6]

Leave to Give Notice to Other Shareholders

Finally, appellant contends that if she failed to establish diversity jurisdiction, "the trial court should have considered the shareholder's request for leave to give notice to the non-Illinois shareholders of Westinghouse . . . " Rule 23.1 provides that a derivative action by a shareholder "shall not be dismissed or compromised without the approval of the court, and notice of the proposed dismissal or compromise shall be given to shareholders or members in such manner as the court directs." The purpose of this rule was stated in 7A Wright & Miller, Federal Practice and Procedure: Civil § 1839, pp. 427-428:

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[6] Appellant also argues that *Navarro Savings Ass'n* v. *Lee*, ____ U.S. ____, 48 L.W. 4551, decided May 19, 1980, after oral argument in this case, and affirming *Lee* v. *Navarro*, 597 F.2d 421 (5 Cir. 1979), is controlling on the "central issue" that the citizenship of an entity rather than that of its shareholders determines jurisdiction in actions based on diversity. In that case the Court held that trustees of a business trust properly invoked diversity jurisdiction on the basis of their own citizenship, regardless of the citizenship of the trust beneficiaries. In holding that the trustees were "real parties to the controversy", the Court noted that the declaration of trust gave the trustees exclusive authority over the property "free from any power or control of the shareholders, to the same extent as if the Trustees were the sole owners . . ." Under these circumstances the citizenship of beneficiaries was not relevant.

We agree with the district court that *Navarro* is inapposite. *Navarro* was an action by the trustees against a third party. It did not involve a dispute or any question of antagonism between the trustees and shareholders. In this case a shareholder is seeking in a derivative action against the corporation to enforce what she believes to be the corporation's right. As the district court found, there is "antagonism" between the shareholder and the corporation. The citizenship of the shareholder under these circumstnaces becomes relevant.

> The notice and court approval of a dismissal or compromise of a shareholder derivative suit is intended to discourage the private settlement of a derivative claim under which a shareholder-plaintiff and his attorney personally profit to the exclusion of the corporation and the other shareholders. Dismissals, as well as settlements, are included in Rule 23.1 to prevent an agreed upon dismissal from being a cloak for a private settlement.
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> . . .
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> . . . On the other hand, it is clear that when the dismissal . . . results from a jurisdictional defect . . . the notice requirement of the rule is not applicable. In [this] situation there is no reason to fear collusion inasmuch as the shareholder-plaintiff's action is being terminated involuntarily.

Id. p. 436.[7]

The notice requirement of Rule 23.1 is not applicable since the dismissal here was involuntary and on jurisdictional grounds.

AFFIRMED.

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[7] See also 3B Moore's Federal Practice, para. 23.124[2]. pp. 130-131; *Marcus* v. *Textile Banking Co.,* 38 F.R.D. 185 (S.D. N.Y. 1965).

APPENDIX B

IN THE UNITED STATES DISTRICT COURT
For the Northern District of Illinois
Eastern Division

EDITH M. MARSCHAK, now known as Edith M. Ashley, as Trustee, on behalf of herself, in such capacity, and on behalf of all others similarly situated,

Plaintiff,

v.

KIRKLAND AND ELLIS, a partnership, and WESTINGHOUSE ELECTRIC CORPORATION,

Defendants.

No. 79 C 1579

MEMORANDUM OPINION AND ORDER

This is a shareholder derivative action brought by Edith Marschak ("plaintiff Marschak"). The complaint alleges that plaintiff Marschak is trustee of a trust which owns stock in Westinghouse Electric Corporation ("Westinghouse"). Plaintiff Marschak has brought the action on behalf of herself, as trustee, and as a representative of all other Westinghouse shareholders. Named as defendants are Westinghouse and Kirkland & Ellis, an Illinois partnership engaged in the practice of law ("Kirkland"). The complaint bases federal jurisdiction on diversity of citizenship under 28 U.S.C. § 1332 (1976). Defendants Westinghouse and Kirkland have moved for dismissal for want of subject matter jurisdiction. As will be indicated herein, complete diversity of citizenship is lacking. Hence, the court lacks subject matter jurisdiction. Defendants' motions, therefore, are granted.

It is well settled that whenever federal jurisdiction is based on diversity of citizenship under 28 U.S.C. § 1332 (1976), there must be complete diversity. "That is, diversity jurisdiction does

not exist unless *each* defendant is a citizen of a different State from *each* plaintiff." *Owen Equipment & Erection Co.* v. *Kroger,* 437 U.S. 365, 373 (1978) (emphasis in original). The burden of proving jurisdiction is, of course, on the party seeking to invoke the court's jurisdiction. Likewise, when diversity is challenged, the burden remains on the party who has alleged diversity. *Village Fair Shopping Center Co.* v. *Sam Broadhead Trust,* 588 F.2d 431, 433 (5th Cir. 1979).

In this action, the complaint does not indicate plaintiff Marschak's state of citizenship. Nor does it indicate defendant Westinghouse's state of incorporation, which is one determinant of a corporation's citizenship. *See* 28 U.S.C. § 1332(c) (1976). It does allege, however, that defendant Kirkland, as an Illinois partnership, is an Illinois citizen and that because defendant Westinghouse's principal place of business is Pennsylvania, it is a Pennsylvania citizen. Further, the complaint states that Westinghouse is the real party in interest and plaintiff Marschak is only a nominal party.

In their motions to dismiss, defendants assert that 1) the complaint is defective for failure to aver facts that clearly show the basis for diversity jurisdiction and 2) because plaintiff Marschak is an Illinois resident, she may be an Illinois citizen, in which case, her citizenship would be the same as that of defendant Kirkland. Thus, diversity would be lacking.

Because jurisdiction is based only on diversity of citizenship, the complaint is defective for failing to allege the parties' citizenship. *See* Rule 8, Fed.R.Civ.P.; *see also Schultz* v. *Cally,* 528 F.2d 470, 473 (3d Cir. 1975). Although these defects might ordinarily be cured by amendment, plaintiff Marschak has had ample opportunity to allege facts showing diversity, which she has not done. Thus, leave to amend will not be granted.

Rather than indicate her state of citizenship, plaintiff Marschak contends that it is irrelevant because Westinghouse is the real party in interest and should be realigned as plaintiff. If

plaintiff Marschak were a nominal party, whose citizenship could be ignored, and Westinghouse were realigned as plaintiff, there would be diversity between Westinghouse, a Pennsylvania citizen, and Kirkland, an Illinois partnership. (Although the complaint does not allege Westinghouse's state of incorporation, later pleadings indicate that it is Pennsylvania. Hence, its state of incorporation, as well as its principal place of business, indicates that Westinghouse is a Pennsylvania citizen.)

The court cannot realign Westinghouse and ignore plaintiff Marschak' citizenship. Realigning the corporation in derivative suits is proper only when it is clear that the cause of action belongs to the corporation and the corporation is not antagonistic to the shareholder. To determine whether there is antagonism between the corporation and the shareholder, the court looks only at the pleadings. *Smith* v. *Sperling,* 354 U.S. 91 (1957).

In this case, the complaint alleges that, pursuant to Rule 23.1, Fed.R.Civ.P., plaintiff Marschak made a demand (that Westinghouse seek recovery from Kirkland) on the Westinghouse Board of Directors. Complaint ¶3 at 2. An amendment to the complaint sets forth in considerable detail, the circumstances that "made it apparent that to await action by the Corporation would have been futile and unavailing." Amendment to the Complaint, ¶4 (filed August 15, 1979).

The corporation's refusal to take action has been held sufficient to show antagonism. *Smith* v. *Sperling,* 354 U.S. 91 (1957); *Rogers* v. *Valentine,* 426 F.2d 1361, 1363 (2d Cir. 1970). Although the complaint here does not specifically allege that the corporation has refused to take action, it does allege essentially that the action taken by the Board of Directors (retaining attorneys) was inadequate. *See* Amendment to the Complaint ¶4 (filed Aug. 15, 1979). Further, plaintiff Marschak has moved to disqualify the Special Investigation Committee, which was appointed by the Board of Directors to

determine whether Westinghouse should assert a claim against Kirkland. It is clear from these pleadings that plaintiff Marschak's view of any action differs from the Board of Directors' view. Hence, there is a sufficient showing of antagonism to preclude realignment. Westinghouse, therefore, must remain a defendant.

Because there is antagonism between defendant Westinghouse and plaintiff Marschak, it is clear that she is more than just a nominal party. Her citizenship, therefore, is relevant. Defendants assert, and plaintiff Marschak has not refuted, that she is an Illinois resident. While residency is not synonymous with citizenship, proof of residency is prima facie evidence of citizenship absent any indication to the contrary. C. Wright, A. Miller, and E. Cooper, *Federal Practice and Procedure* § 3611 at 711-12 (citing *Kelleam* v. *Maryland Casualty Co.,* 112 F.2d 940, 943 (10th Cir. 1940), *rev'd. on other grounds,* 312 U.S. 377 (1941); *Howard* v. *Barr,* 114 F.Supp. 48, 50 (W.D. Ky. 1953). As plaintiff Marschak has neither stated her citizenship, nor denied that she is an Illinois resident, the court must conclude that she is an Illinois citizen. Because defendant Kirkland also has Illinois citizenship, complete diversity is lacking. Accordingly, defendants' motions to dismiss are granted. The complaint is dismissed without prejudice.

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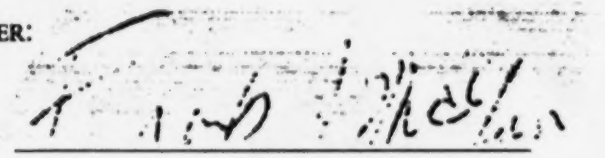

United States District Judge

DATED: December 7, 1979

IN THE UNITED STATES DISTRICT COURT
For the Northern District of Illinois
Eastern Division

EDITH M. MARSCHAK, now known as Edith M. Ashley, as Trustee, on behalf of herself, in such capacity, and on behalf of all others similarly situated,

Plaintiff,

v.

KIRKLAND AND ELLIS, a partnership, and WESTINGHOUSE ELECTRIC CORPORATION,

Defendants.

No. 79 C 1579

MEMORANDUM OPINION AND ORDER

On November 27, 1979, this court announced its decision on defendants' motions to dismiss. Finding that diversity of citizenship was lacking, the court dismissed the complaint for want of subject matter jurisdiction. Before the Memorandum Opinion and Order was issued, plaintiff Marschak filed a motion seeking reconsideration and a stay of the Westinghouse Special Investigation Committee's report, or, alternatively, leave to send a notice to other shareholders advising them of the dismissal and inviting them to substitute as plaintiffs. The court has reconsidered the ruling on the motions to dismiss and finds that, because diversity is still lacking, the court does not have jurisdiction. Accordingly, plaintiff's instant motions are denied. The basis for this ruling follows.

Plaintiff's motion to reconsider is based on the Fifth Circuit's ruling in *Lee* v. *Navarro Savings Association,* 597 F.2d 421 (5th Cir. 1979), *cert. granted,* 48 U.S.L.W. 3349 (U.S. Nov. 26, 1979) (No. 79-465). In that case, the trustees of a

business trust brought a breach of contract action, on behalf of the trust, against a savings association. The Court of Appeals for the Fifth Circuit held that because the trustees were vested with the power to sue and be sued on behalf of the trust and were in actual control of the trust, they were the real parties in interest whose citizenship was considered for diversity purposes. 597 F.2d at 425. In holding that the trust beneficiaries' citizenship was irrelevant, the court relied on the Declaration of Trust which gave broad powers to the trustees and strictly limited the beneficiaries' rights. *Id.* at 424-25. Thus, the court found that the trustees possessed "the sole right to bring [the] action." *Id.* at 425.

The instant case differs from *Navarro* in that Westinghouse is not a business trust, but a corporation. This is a derivative action, which by its unique nature indicates that the corporation is not "exclusively entitled to enforce [its] rights." *Id.* at 424. Unlike the beneficiary of the business trust in *Navarro,* the shareholder in a derivative action can enforce what he believes to be the corporation's right. *Navarro,* therefore, is not controlling here and this court's earlier decision dismissing the complaint remains in effect.

Because the court does not have jurisdiction, it cannot stay the issuance of the Special Investigation Committee's report or grant leave to send a notice to the other shareholders. Accordingly, plaintiff's motion is denied *in toto.*

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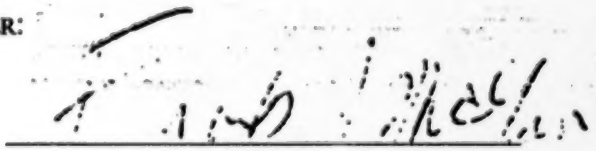

United States District Judge

DATED: December 7, 1979

APPENDIX C

LAW OFFICES
MARSHALL PATNER
10 SOUTH LA SALLE STREET
CHICAGO, ILLINOIS 60603
(312) 236-7091

March 13, 1979

Mr. Robert E. Kirby
Chairman of the Board of Directors
Westinghouse Electric Corporation
Gateway Center Westinghouse Building
Pittsburgh, Pennsylvania 15222

Dear Mr. Kirby:

I am writing to you as attorney for a shareholder of the Westinghouse Electric Corporation. I am writing to make a demand on the Board of Directors of the Corporation, in compliance with Rule 23.1 of the Federal Rules of Civil Procedure, to file suit in the name of the Corporation against the law firm of Kirkland & Ellis. The demand is made on you to seek recovery of all legal fees, costs and incidental expenses, and for damages, actual, punitive and exemplary and for fees, for the amounts paid to the law firm for the litigation known as *Westinghouse Electric Corporation* v. *Kerr-Mc Gee Corporation, Gulf Oil Corporation and Getty Oil Company.* This case was brought in the Northern District of Illinois, Eastern Division, and on appeal the United States Court of Appeals for the Seventh Circuit decided that the law firm was disqualified from representing the corporation in the litigation because of a conflict of interest. This demand includes a request to seek recovery of all amounts paid to the firm for its unsuccessful defense of its position denying the conflict.

It is imperative that you instigate this litigation against Kirkland & Ellis with immediate dispatch in order to protect the interest of the Corporation, and of the stockholders similarly situated to my client, and to prevent any further harmful consequences because of the firm's action. I therefore ask you for written assurance within thirty days of the date of this letter that such litigation will be undertaken in the name of the corporation; otherwise, upon failure of the Board of Directors to do so, my client, who was a shareholder during all times relevant to this demand, has instructed me to promptly institute a derivative action. I am sending copies of this demand letter individually to each member of the Board of Directors, care of the Corporation.

I will be pleased to meet with independent counsel, if I am first given a full opportunity to examine your memoranda on the subject, with a view toward eliminating the directors as potential defendants. I look forward to your reply.

Yours very truly,

/s/ Marshall Patner

Marshall Patner

APPENDIX D

Westinghouse
Electric Corporation

Robert F Pugliese
Vice President
and General Counsel, Secretary

Westinghouse Building
Gateway Center
Pittsburgh Pennsylvania 15222

April 9, 1979

Marshall Patner, Esquire
10 South LaSalle Street
Chicago, Illinois

Re: Westinghouse Electric Corporation v.
Kerr-McGee Corporation, et al.

Dear Mr. Patner:

I have been asked to respond to your recent letters dated March 13, 1979 in connection with the above matter.

Some months prior to receipt of your letter, Westinghouse Electric Corporation ("Westinghouse") retained the Pittsburgh law firm of Eckert, Seamans, Cherin & Mellott as independent counsel to conduct a review of the matter of the disqualification of the law firm of Kirkland & Ellis as counsel for Westinghouse in its anti-trust suit against twenty-nine uranium producers and to advise Westinghouse with respect to the rights which it might have as a result of that disqualification. We have had several discussions with members of the Eckert firm with respect to this matter and have received and reviewed with the Board of Directors the tentative conclusions of that firm.

Please be assured that once the Eckert firm has completed its review and Westinghouse has had a reasonable opportunity to consider the recommendations, we shall communicate with you.

In conclusion, I would like to point out, however, that Kirkland & Ellis, without admitting any liability to do so, has agreed that Westinghouse shall not be required to pay the costs and fees associated with the defense by Kirkland & Ellis in the disqualification proceedings.

Sincerely,

R. J. Bruglieri